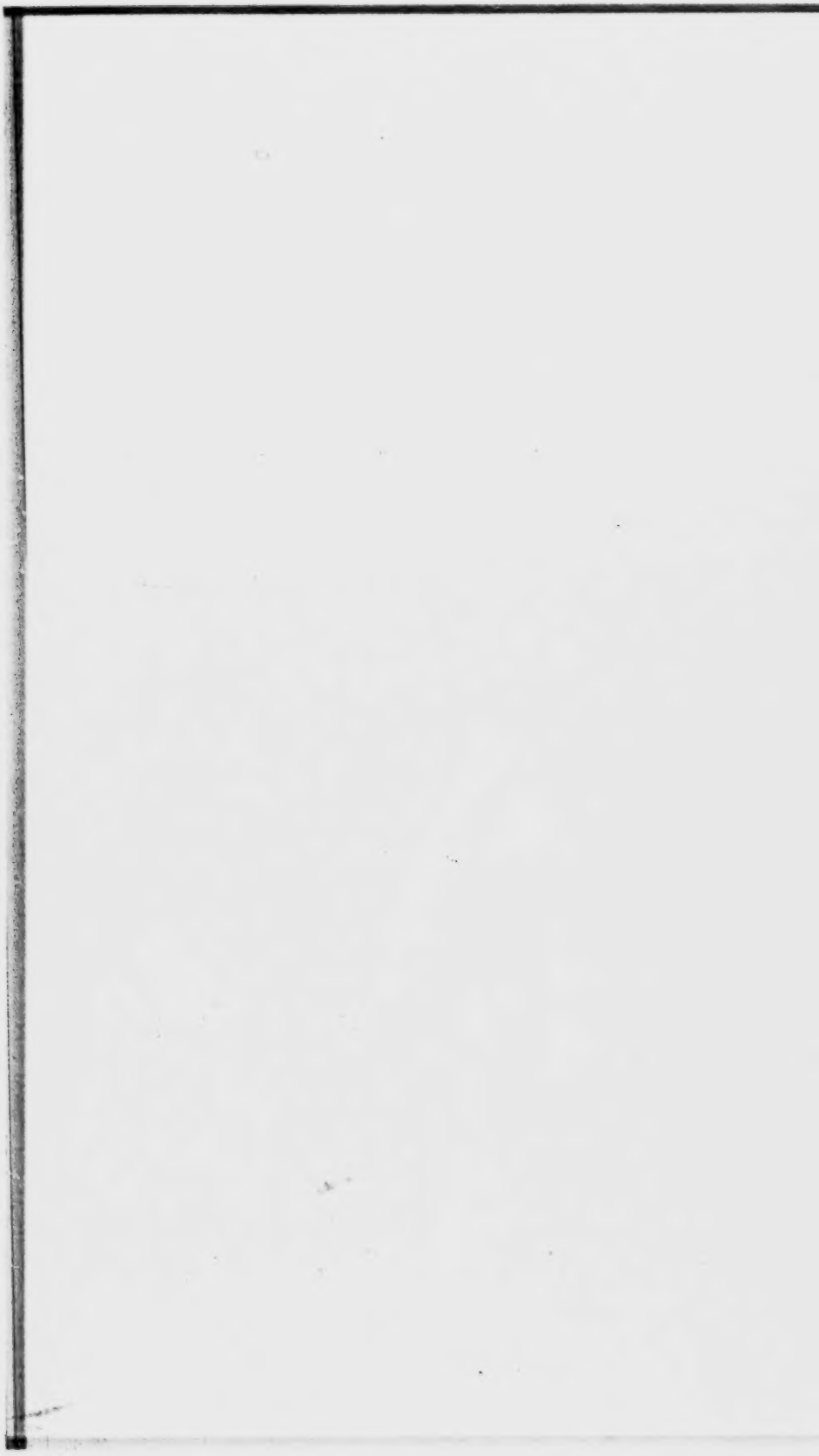

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CHARLES ELMORE
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1933.

No. 909 No. 910

DETROIT TRUST COMPANY, TRUSTEE,
Petitioner,

against

Steamer THOMAS BARLUM, her engines, etc., Barlum Steamship Company,
Respondent.

DETROIT TRUST COMPANY, TRUSTEE,
Petitioner,

against

Steamer JOHN J. BARLUM, her engines, etc., Barlum Steamship Company,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF.

RAY M. STANLEY,
ELLIS H. GIDLEY,
FERRIS D. STONE,
Counsel for Petitioners.

BATAVIA TIMES, LAW PRINTERS,
BATAVIA, N. Y.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1933.

No.....

DETROIT TRUST COMPANY, TRUSTEE,
Petitioner,

against

Steamer THOMAS BARLUM, her engines, etc., Barlum Steamship Company,
Respondent.

DETROIT TRUST COMPANY, TRUSTEE,
Petitioner,

against

Steamer JOHN J. BARLUM, her engines, etc., Barlum Steamship Company,
Respondent.

THE PETITION OF DETROIT TRUST COMPANY, TRUSTEE, FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Petition.

Your petitioner, Detroit Trust Company, Trustee, mortgagee named in each of two preferred marine

mortgages covering the Steamers *Thomas Barlum* and *John J. Barlum,* respectively, prays that a writ of certiorari issue to the United States Circuit Court of Appeals for the Second Circuit to review its orders entered in the above entitled causes on February 13th, 1934 (R. 336-338) reversing the decrees of the United States District Court for the Western District of New York. Neither the prevailing nor dissenting opinions of the Circuit Court of Appeals (R. 324-329, 330-336) are yet officially reported. The original opinion of the District Court upon exceptions (R. 120-121) is reported at 56 Fed. (2d) 455, and the subsequent opinion of the District Court following trial of the causes (R. 264-267) is reported at 2 Fed. Supp. 733.

Nature of the Case.

These suits in admiralty, tried together, were instituted by petitioner for the foreclosure, following default, of two preferred marine mortgages covering the Steamers *Thomas Barlum* and *John J. Barlum,* respectively, given pursuant to the Ship Mortgage Act (Act June 5, 1920, Chap. 250, Sec. 30; 41 Stat. 1000-1006; 46 U. S. C. Chap. 25). The suits were resisted on the ground that the proceeds of the mortgages being largely intended and used for non-maritime purposes no maritime lien subject to admiralty jurisdiction arose therefrom, and that the Ship Mortgage Act 1920, insofar as it purports to permit the foreclosure of such mortgages by suit *in rem* in admiralty and to grant original jurisdiction of such suits to the District Courts of the United States is violative of and in contravention of Article III, Section 2, of the Consti-

tution of the United States and is null, void and of no effect (R. 124-125).

Full compliance with all statutory requirements to make each mortgage a preferred mortgage under the Ship Mortgage Act is admitted by the respective answers.

Each preferred mortgage was given to secure payment of a loan of $200,000 made by Detroit Trust Company to the vessel owner. Each loan was evidenced by an issue of bonds aggregating that sum and maturing serially. The bond issues were purchased by Detroit Trust Company for sale to the general public and were largely so sold. Default occurred in payment of each issue of bonds, whereupon libelant invoked the jurisdiction of the District Court, pursuant to Subsection K of the Ship Mortgage Act (41 Stat. 1003; 46 U. S. C. Sec. 951) for the enforcement of the lien of each preferred mortgage.

John J. Barlum was the principal and controlling owner of stock in the mortgagor corporation when the mortgages in suit were negotiated and delivered (R. 196-199, 250).

Of the proceeds of the mortgage given on the *Thomas Barlum*, the testimony, which is without dispute, shows that the Detroit Trust Company (Mortgagee, Trustee) disbursed the proceeds of the mortgage in exact conformity with the written directions supplied by the mortgagor, as follows:

$50,358.33 for the refunding of the unpaid balance of a prior existing mortgage, also exe-

cuted and delivered under the provisions of the Ship Mortgage Act.

$45,510.00 for the payment of a note of Thomas Barlum & Sons (a corporation controlled by John J. Barlum, President of the mortgagor).

$54,490.00 for the payment of two notes of John J. Barlum.

$ 1,545.23 for the payment of miscellaneous expenses in connection with the giving of the mortgage.

$42,896.44 the residue, was paid to the mortgagor (R. 231).

Of the proceeds of the *John J. Barlum* mortgage, there is nothing in the record to indicate that the Detroit Trust Company (Mortgagee, Trustee) had advance knowledge of the manner in which the balance of the proceeds of the mortgage turned over to the mortgagor and amounting to substantially more than half such proceeds were to be used. After the mortgage was executed, delivered and recorded, the Detroit Trust Company (Mortgagee, Trustee) disbursed the moneys in exact conformity with the express directions in writing of the mortgagor, as follows:

$ 92,363.38 for the payment of note, bonds and coupons of John J. Barlum.

After deduction of miscellaneous expenses connected with the mortgage, there was paid to the mortgagor a balance of

$102,801.55 (R. 240).

The testimony fairly shows that the several amounts paid to others than the mortgagor, as indicated, were

paid by the express direction of the mortgagor and merely constituted loans made by the mortgagor out of the proceeds (R. 194, 207).

The libels respectively allege the execution and delivery of the preferred mortgages (as intended to be such) to secure payment of the indebtedness evidenced by each bond issue. A complete and strict compliance with the Ship Mortgage Act is alleged. Default is pleaded and relief is sought by sale of the respective vessels and decree of foreclosure thereon (R. 12-15, 66-69).

Upon the filing of the libels and seizure of the respective vessels at the Port of Buffalo, Barlum Steamship Company made claim thereto and attacked the jurisdiction of the District Court through exceptions. After hearing, the exceptions were overruled by the District Court (R. 123). Claimant then interposed answers which *admit* every allegation of the libels. Two separate defenses are therein alleged; the first of which alleges that the proceeds of the loans, as evidenced by an issue of bonds to secure payment of which the respective mortgages were given, were used by claimant (Mortgagor) almost entirely for non-maritime purposes to the knowledge of libellant when the mortgages were executed and delivered. The second defense is the same as was urged by exceptions (R. 124-125).

Testimony was taken and trial of both causes had upon the issue raised by such first defense. A further opinion was filed by the District Court upholding the

right to enforce the respective preferred mortgages in a Court of Admiralty as provided by the Ship Mortgage Act. Decrees were entered in the respective suits providing for foreclosure and directing the sale of the vessels to satisfy the amounts found to be due (R. 268, 280). Claimant appealed and the Circuit Court of Appeals, by a divided court, reversed the decrees of the District Court. Petitions for rehearing were subsequently denied (R. 338, 339).

In determining that the jurisdiction provided by the Ship Mortgage Act did not extend to the mortgages at bar, the prevailing opinion of the Circuit Court of Appeals (Manton and Chase, C. J.) held:

1. That the jurisdiction of the District Court over an action *in rem* to foreclose a preferred mortgage complying with all the express provisions of the Ship Mortgage Act may be collaterally attacked by the mortgagor and jurisdiction defeated by showing that the mortgagor and mortgagee had advance knowledge that a substantial part of the proceeds of the mortgage were to be used for non-maritime purposes.

2. That the result follows notwithstanding the libel alleges and the answer admits that the mortgage in question is a preferred mortgage under the Act.

3. That admiralty jurisdiction over the foreclosure of preferred mortgages on vessels is limited to mortgages the proceeds of which were used "to develop and encourage the maintenance of a merchant marine" (R. 324-329).

Petitioner contended below, and now contends, that this construction is an unwarranted and narrow limita-

tion of the Ship Mortgage Act, and that the correct construction is that set forth in the dissenting opinion of the Circuit Court of Appeals (A. N. Hand, C. J.) which held:

1. That since each mortgage admittedly was a valid mortgage, and since the owner (Mortgagor) in all respects complied with the provisions of the Ship Mortgage Act relating to preferred mortgages, each mortgage attained a preferred status.

2. That the Ship Mortgage Act was passed in aid of the development and encouragement of our merchant marine, and was intended to give to ship mortgages complying with the statute a status permitting their more advantageous employment by way of promotion of investment than had been theretofore enjoyed.

3. That to make the status of a preferred mortgage depend upon the purposes for which it is given is to engraft upon the plain words of the statute an exception seemingly contrary to its terms and not required by any convincing public policy.

4. That the whole matter is one of the creation and displacement of liens upon ships as essential marine instrumentalities over which Congress has complete control under its power to alter, qualify or supplement the maritime law.

5. That the mortgages in suit being admittedly valid as preferred mortgages, the admiralty court had jurisdiction and the decrees ordering sales of the vessels for the satisfaction of the liens of the mortgages should be affirmed (R. 330-336).

Questions Presented.

1. Was it the intention of Congress in enacting Subsection K of the Ship Mortgage Act to withhold jurisdiction of an action *in rem* brought to foreclose a preferred mortgage in all cases where the mortgagor and mortgagee knew in advance that a substantial part of the proceeds was to be devoted to non-maritime uses?

2. Can jurisdiction of a District Court over an action *in rem* brought under Subsection K of the Ship Mortgage Act be defeated without destroying the status of a mortgage as a preferred mortgage under the Ship Mortgage Act?

3. If Congress intended to create a preferred mortgage lien in all cases where the provisions of the Ship Mortgage Act are strictly complied with, irrespective of the devotion of the proceeds to non-maritime uses, has it the power so to do under Article III, Section 2 of the Constitution?

The Ship Mortgage Act is unconditional in form. By Subsection D (41 Stat. 1000, 46 U. S. C. Sec. 922) it is provided:

> "(A) A valid mortgage which, at the time it is made includes the whole of any vessel of the United States of 200 gross tons and upward, shall in addition have, in respect to such vessel and as of the date of the compliance with all the provisions of this subdivision, the preferred status given by the provisions of Subsection M, if—"

then follow various conditions with respect to endorsement, recording, filing of affidavit, etc., compliance

with which is essential for the attaining of the status of a preferred mortgage.

Subsection E of the Ship Mortgage Act (41 Stat. 1001, 46 U. S. C. Sec. 923) further requires the procuring of certified copies of the preferred mortgage following recording and the retention of one such copy on board the mortgaged vessel for purposes of exhibition to any person having business with the vessel which may give rise to a maritime lien.

Each libel alleges a complete and strict compliance with all the provisions of the Ship Mortgage Act requisite to give to the respective mortgages the preferred status accorded by the statute. Each answer specifically *admits* that every allegation of the libel is true.

That, upon compliance with all the conditions specified, the mortgage is made preferred, is the enunciated doctrine of this Court in the only cause involving the Ship Mortgage Act which has come before it.

Morse Dry Dock & Repair Company v. Steamship The Northern Star, 271 U. S. 552, 556.

In that case the constitutionality of the Ship Mortgage Act appears to have been assumed, although seemingly not directly presented for decision.

However, several decisions of the District Courts have considered at length and have sustained the constitutionality of the Act as well as the power of Congress to enlarge the jurisdiction of the District Court sitting in admiralty.

The Oconee, 280 F. 927 (E. D. Virginia);
The Nanking, 292 F. 642 (N. D. Cal.);
The Lincoln Land, 295 F. 358 (D. Mass.).

Other decisions of Federal Courts have plainly assumed the validity of the Ship Mortgage Act and of preferred mortgages complying therewith.

The Egeria, 294 F. 791 (C. C. A. 9);
The Northern Star, 7 F. (2d) 505 (C. C. A. 2);
National Bank v. Enterprise Marine Dock Co., 43 F. (2d) 547, (C. C. A. 4);
Consumer's Co. v. Goodrich Transit Co., 53 F. (2d) 972 (C. C. A. 7); cert. denied 286 U. S. 548;
The Owego, 292 F. 403 (E. D. La.);
The Northern, No. 41, 297 F. 343 (S. D. Florida);
The Moshulu, 298 F. 348 (N. D. Cal.);
The Henry W. Breyer, 17 F. (2d) 423 (D. Maryland);
The Red Lion, 22 F. (2d) 329 (E. D. N. Y.).

Petitioner contends where it is conceded that the mortgage was valid and where all the statutory requirements requisite to accord such mortgage preferred status were complied with that such preferred mortgage, by virtue of the statutory provision, constitutes a preferred mortgage lien upon the mortgaged vessel. Petitioner also contends that upon default occurring in the terms or conditions of a preferred mortgage, such lien is enforceable by the mortgagee by suit *in rem* in admiralty, of which suit exclusive original jurisdiction is granted to the District Courts of the United States by virtue of Subsection K of the Ship Mortgage Act (41 Stat. 1003, 46 U. S. C. Sec. 951).

Exclusive original jurisdiction having been conferred upon the District Courts for the enforcement

of a lien created by the Ship Mortgage Act upon vessels of the United States over which Congress has undeniable power, petitioner contends that such jurisdiction is absolute and positive in every case where such preferred mortgage lien is existent by reason of compliance with the conditions of the Ship Mortgage Act.

The majority decision of the Circuit Court of Appeals is based upon the erroneous proposition that, although the mortgages were admittedly valid as preferred mortgages within the purview of the Ship Mortgage Act, the statutory grant of jurisdiction over the enforcement of the lien thereby created failed once it appeared that the mortgagee had advance knowledge that the mortgagor intended to, and did, use a substantial portion of the proceeds of the borrowings for non-maritime purposes.

The majority opinion said:

> "It is not enough to say that they were mortgages with due formalities placed upon the vesvels. As soon as it appeared at the trial, and it did so beyond question, that the loan was not made to be used for purposes of navigation or relating to things maritime, the court should have declined jurisdiction" (R. 329).

The majority opinion ignores the fact that the mortgages were each made after proper corporate action authorizing their execution under resolutions asserting that it was necessary to borrow the moneys "for the use and benefit" of the respective vessels (R. 253, 258). Similarly, the majority opinion overlooks completely the covenants of the mortgagor contained in

the respective mortgages that the mortgagor shall comply with and satisfy all the provisions of the Ship Mortgage Act and "shall establish and maintain this mortgage as a first preferred mortgage under said Act" (R. 35, 88). Further while admitting that the Ship Mortgage Act does not say anything about how the proceeds of the loan secured by the mortgage are to be used, the majority opinion of the Circuit Court of Appeals flatly holds that a maritime use was contemplated. Hence, the majority opinion, through reliance upon facts *aliunde* the instruments themselves relating to how the moneys thus secured were to be spent, determined that the District Court is without jurisdiction in the present suits and that the petitioner must be relegated to its remedy at common law.

Reasons for Allowance of Writ.

1. The questions presented are of considerable public importance which have not been, but should be, settled by this Court, involving fundamental questions of jurisdiction in admiralty. Indeed, the questions actually go deeper, in that while the Circuit Court of Appeals placed its decision on a basis of statutory construction, the underlying question is a constitutional one. If the statute includes within its terms the preferred mortgages in suit, as petitioner contends it clearly does, then it must be determined whether the Constitution, Article III, Section 2, permits such expansion of the field of admiralty. The constitutional problem was recognized and argued by counsel for the parties and is squarely dealt with by the dissenting opinion.

If Congress had the power under Article III, Section 2 of the Constitution to amend the general maritime

law as expressed in the Ship Mortgage Act, Subsection K of the same Act, extending the jurisdiction of the District Court, is equally valid. If, by strict compliance with the Act, each mortgage in suit became a preferred mortgage under the Act, the jurisdiction of the District Court over an action to foreclose automatically follows. It, therefore, results that the jurisdiction of the District Court over an action *in rem* to foreclose can only be defeated by destroying the preferred character of the mortgage.

The strained and illiberal construction of the statute by the majority opinion of the Circuit Court of Appeals is the result of an attempt to avoid the onus of declaring the statute in violation of the Constitution. The decision in these cases is of great interest and importance to all persons interested in our national shipping and its financing. The fostering of a merchant marine has been the fixed policy of our government for many years.

2. Throughout the country there are numberless holders of bonds secured by preferred mortgages under the Ship Mortgage Act. The decision of the majority of the Circuit Court of Appeals has opened wide the door to an attack on preferred mortgages as such and thus has impaired the value of such bonds as a security with a possibility of their complete destruction in individual cases. The pernicious effect on future efforts to float bond issues secured by preferred mortgages is certain. It follows that if this decision stands the purpose of Congress in enacting the Ship Mortgage Act will be defeated.

3. The decision in the present case is contrary both to the letter and the spirit of the Ship Mortgage Act.

It nullifies the provisions for the enforcement of the lien created by the statute by imposing upon the plain words of the statute a condition which is wholly irrelevant;—namely, to what uses did the mortgagor with the knowledge of the mortgagee put the moneys obtained upon the security of the instruments. In so determining, the Circuit Court of Appeals expressly refrained from deciding whether a loan made for maritime purposes secured by a mortgage upon a ship will become non-maritime if the borrower, contrary to the agreement of the mortgage, diverts the money to non-maritime purposes; nor would the Court express itself as to the effect, in such case, of estoppel. But the Court clearly bases its decision upon the advance knowledge of the mortgagee as to the ultimate non-maritime use of a substantial part of the borrowings by the mortgagor which depends on testimony wholly *dehors* the instrument offered for the purpose of controverting the express covenants of the mortgage. Such a construction finds no support in the letter of the Ship Mortgage Act and is contrary to the intent of Congress in the enactment of the measure for the creating of valid mortgage security on ships which would thus be made the subject of investment.

4. The Circuit Court of Appeals is in palpable error in holding that jurisdiction is to be determined by the purely subjective test of knowledge of the mortgagee of the intended use of the funds loaned.

5. The majority decision of the Circuit Court of Appeals is based upon a misapplication of the decisions of this Court in

Bogart v. The Steamboat John Jay, 17 How. 399;

Schuchardt v. Babbage, 19 How. 239;
Peoples' Ferry Co. v. Beers, 20 How. 393;
The Lottawanna, 21 Wall. 558;
The J. E. Rumbell, 148 U. S. 1.

We respectfully submit that the decision of the Circuit Court of Appeals is wrong and should be reviewed by this Court.

WHEREFORE, your petitioner prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the United States Circuit Court of Appeals for the Second Circuit commanding that Court to certify and send to this Court for its review and determination on a day certain to be named therein, a full and complete transcript of the record and all the proceedings in the cases numbered on its docket numbers 175-176, October Term 1933, and entitled: "Detroit Trust Company, Trustee, Libelant-Appellee, against Steamer *Thomas Barlum,* her engines, etc., Barlum Steamship Company, Claimant-Appellant; Detroit Trust Company, Trustee, Libelant-Appellee, against Steamer *John J. Barlum,* her engines, etc., Barlum Steamship Company, Claimant-Appellant", and that the said decrees of the United States Circuit Court of Appeals for the Second Circuit may be reversed by this Honorable Court, and that your petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just, and your petitioner will ever pray.

DETROIT TRUST COMPANY, TRUSTEE,
Petitioner.

RAY M. STANLEY,
ELLIS H. GIDLEY,
FERRIS D. STONE,
Counsel for Petitioner.

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1933.

No.

DETROIT TRUST COMPANY, Trustee,
Petitioner,

against

Steamer THOMAS BARLUM, her engines, etc., BARLUM STEAMSHIP COMPANY,
Respondent.

DETROIT TRUST COMPANY, Trustee,
Petitioner,

against

Steamer JOHN J. BARLUM, her engines, etc., BARLUM STEAMSHIP COMPANY,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

Jurisdiction.

This is a suit within the admiralty and maritime jurisdiction of the United States and of this Honorable Court. Jurisdiction is invoked under Article III, Section 2 of the Constitution of the United States of America, and under Section 240 of the Judicial Code

as amended by the Act of February 13th, 1925, 43 Stat. 938 (U. S. C. A., Title 28, Section 347).

Statement.

The majority of the essential facts are stated in the petition and will not be repeated here. We call attention, however, to the fact that the testimony upon which the majority opinion of the Circuit Court of Appeals was based was all admitted over the objection and exception of libelant (R. 133-134). This testimony in substance merely amounts to this—that the mortgagor loaned a substantial portion of the proceeds of each mortgage to third parties *(i. e.,* the President of the mortgagor and to corporations controlled by him). These borrowers in turn used the moneys for non-maritime purposes. The borrowers were charged on the books of the mortgagor with the amount of the loans (R. 194, 207), obviously with the expectation that the loans would be repaid in due course.

Specifications of Error.

The Circuit Court of Appeals erred in the following:

1. In holding that it was the intention of Congress in enacting Subsection K of the Ship Mortgage Act to withhold jurisdiction of an action *in rem* brought to foreclose a preferred mortgage in all cases where the mortgagor and mortgagee knew in advance that a substantial part of the proceeds was to be devoted to a non-maritime use.

2. In holding that the jurisdiction of a District Court over an action *in rem* brought under Subsection

K of the Ship Mortgage Act may be defeated without destroying the status of a mortgage as a preferred mortgage under the Ship Mortgage Act.

3. In holding that strict compliance with all the express provisions of the Ship Mortgage Act does not of itself vest jurisdiction in the District Court over an action *in rem* to foreclose the mortgage, but that jurisdiction may be defeated by testimony *aliunde* that the loan was not made to be used for purposes of navigation or relating to things maritime.

4. In reversing the decrees of the District Court directing foreclosure and sale of the mortgaged vessels as prayed for in the libels.

POINT I.

The Ship Mortgage Act contains no express or implied condition that the proceeds of a preferred mortgage shall be devoted to maritime uses. Therefore, an intention to use the proceeds of such a mortgage for non-maritime purposes cannot affect the status of the mortgage, or the jurisdiction of the District Court to enforce it.

The language of the Ship Mortgage Act is precise, definite and certain. By Subsection D (41 Stat. 1000; 46 U. S. C. Sec. 922) it provides:

> "(a) A valid mortgage which, at the time it is made includes the whole of any vessel of the United States of 200 gross tons and upward, shall in addition have, in respect to such vessel and as of the date of the compliance with all the provi-

sions of this subdivision, the preferred status given by the provisions of subsection M, if—

(1) The mortgage is indorsed upon the vessel's documents in accordance with the provisions of this chapter;

(2) The mortgage is recorded as provided in Subsection C, together with the time and date when the mortgage is so indorsed;

(3) An affidavit is filed with the record of such mortgage to the effect that the mortgage is made in good faith and without any design to hinder, delay, or defraud any existing or future creditor of the mortgagor or any lienor of the mortgaged vessel;

(4) The mortgage does not stipulate that the mortgagee waives the preferred status thereof; and

(5) The mortgagee is a citizen of the United States.

(b) Any mortgage which complies in respect to any vessel with the conditions enumerated in this subsection is hereafter in this chapter called a 'Preferred Mortgage' as to such vessel.

(c) There shall be indorsed upon the documents of a vessel covered by a preferred mortgage—

(1) The names of the mortgagor and mortgagee;

(2) The time and date the indorsement is made;

(3) The amount and date of maturity of the mortgage; and

(4) Any amount required to be indorsed by the provisions of subdivision (e) or (f) of this subsection.

> (d) Such indorsement shall be made (1) by the collector of customs of the port of documentation of the mortgaged vessel, or (2) by the collector of customs of any port in which the vessel is found, if such collector is directed to make the indorsement by the collector of customs of the port of documentation; and no clearance shall be issued to the vessel until such indorsement is made. * * *."

It is to be observed that the statute has enumerated in complete and precise detail, every step to be taken in order that the mortgage may attain the preferred status created by the Act. Strict compliance with every requirement of the Act is, therefore, necessary.

The mortgage having attained a preferred status, through strict compliance with the Act, Subsection K (41 Stat. 1003; 46 U. S. C. Sec. 951) provides that:

> "A preferred mortgage shall constitute a lien upon the mortgaged vessel in the amount of the outstanding mortgage indebtedness secured by such vessel."

Subsection M (41 Stat. 1004, 46 U. S. C. Sec. 953) provides that upon a sale of any mortgaged vessel by order of a District Court in any suit *in rem* in admiralty for the enforcement of a preferred mortgage lien thereon:

> "(b) * * * the preferred mortgage lien shall have priority over all claims against the vessel, except (1) preferred maritime liens; and (2) expenses and fees allowed and costs taxed, by the Court."

The libels in these cases allege a full and complete compliance with every provision of the Ship Mortgage Act necessary to make the mortgages in suit preferred mortgages under the Act. The answers interposed *admit* that every act and thing necessary to be done was done to make these mortgages preferred mortgages under the Act, and further expressly *admit* that the mortgages are preferred mortgages under the Act.

The majority opinion of the Circuit Court of Appeals in these cases has, for the first time, grafted on to the Ship Mortgage Act, a further condition not warranted by the language of the Act, and which would seem to be negatived by the express terms of the Act. This condition imposed by the court below, in effect, is that no matter how strict the compliance with the express provisions of the Act, if the intention existed, known to both mortgagor and mortgagee, to devote a substantial portion of the proceeds to non-maritime uses, the preferred status is not attained, at least insofar as jurisdiction of the District Court is concerned. This construction is certainly anomalous for the reason that it makes jurisdiction of a District Court in an action brought to foreclose a mortgage depend upon advance knowledge of a fact rather than upon the fact itself.

That Congress did not intend to impose any implied limitations on the use of the proceeds is fairly evidenced by the express provisions of paragraph (e) of Subsection D of the Act (41 Stat. 1000; 46 U. S. C. Sec. 922, par. (e) which provides:

> "(e) A mortgage which includes property other than a vessel shall not be held a preferred mort-

> gage unless the mortgage provides for the separate discharge of such property by the payment of a specified portion of the mortgage indebtedness. If a preferred mortgage so provides for the separate discharge, the amount of the portion of such payment shall be indorsed upon the documents of the vessel."

By this section Congress has expressly provided for a single mortgage covering ships together with any other conceivable form of property, and provides that the only requirement necessary to be observed for the maintenance of the mortgage as a preferred mortgage on the vessel shall be a provision contained in the mortgage providing for a separate discharge of such other property by the payment of a specified portion of the mortgage indebtedness and by the endorsement on the ship's papers of the amount so required to be paid.

It is obvious that Congress contemplated no allocation of the proceeds of such a mortgage to specific uses. If such had been the intention of Congress, unquestionably express provision therefor would have been incorporated in the statute.

The conclusion of the majority of the Circuit Court of Appeals, therefore, is not based upon the language of the statute, but is based upon the assumption that Congress is without power to create a preferred mortgage lien over which the District Court, sitting in admiralty, would have jurisdiction unless the mortgage lien so created was made expressly "for navigation or shipping purposes within the statute." Such a construction conflicts with the intention of Congress as

expressed in paragraph (e) of Subsection D of the Act (41 Stat. 1000; 46 U. S. C. Sec. 922, par. (e)); and no other provision of the Ship Mortgage Act lends support to the conclusion reached.

The majority opinion of the Circuit Court of Appeals defeats jurisdiction of the District Court upon the single ground that the mortgagor and mortgagee had knowledge at the time the mortgages were executed that a substantial part of the proceeds were to be devoted to non-maritime uses and assumes the constitutionality of the Act upon the ground that:

> "It was not the intention of Congress, by the mere grant of jurisdiction under the terms of the Ship Mortgage Act, to confer jurisdiction on the federal court to foreclose a mortgage lien placed on the vessel which was not made a maritime lien for navigation or shipping purposes within the statute. In granting such jurisdiction, Congress could have intended only a valid preferred mortgage thus authorized to be made under the terms of the Ship Mortgage Act. It must be a transaction which relates to navigation and things maritime" (R. 329).

Assuming this to be the intention of Congress, the Circuit Court of Appeals has thus made a practical construction of the Act, and so construing it, has held that jurisdiction of the District Court in the instant causes fails because of the use of a substantial part of the proceeds of the mortgages for non-maritime purposes. Continuing, the Court holds that the intention of Congress being plain, a mortgage executed and delivered under the precise circumstances here dis-

closed cannot attain such a preferred status as to give a District Court jurisdiction over an action *in rem* for its enforcement, and that the only way in which a mortgage executed and delivered under the precise circumstances here disclosed can attain such a status will be by an act of Congress making the necessary extension of the Ship Mortgage Act. This is evidenced by the following language employed by the majority decision below:

> "In the absence of an express provision, The Ship Mortgage Act will not be construed to extend to such a case" (R. 328).

Thus the Court affirms the constitutionality of the Ship Mortgage Act based upon an assumed intention of Congress which finds no support in the Act itself and at the same time defeats the jurisdiction of the District Court to enforce the mortgages in suit. It is to be observed that such defeat of jurisdiction is based solely upon the mere existence of knowledge that some part of the moneys were to be diverted to non-maritime uses. That jurisdiction of the District Court, sitting in admiralty, cannot be defeated except by the destruction of the preferred status of the mortgages we will discuss in a later point.

The motive and intention of Congress in enacting the legislation in question is not only clearly evidenced in the *Senate* Reports, Volume I, 66th Congress 2nd Session, but is also expressly set forth in Section I of the Merchant Marine Act of 1920 (Act of June 5, 1920, Ch. 250, Sec. 1; 41 Stat. 988; 46 U. S. C. Sec. 861) of which the Ship Mortgage Act is a part. From the Senate Reports and the recital in Section I of the Act,

it appears that the purpose of the Act was to stimulate the building of ships and the investment of capital therein. The broad purpose of Congress cannot be better expressed than by quoting the language contained in the dissenting opinion of Judge Hand in which he said:

> "It may well be that the building of ships and the investment of capital therein can best be promoted by allowing vessels to be hypothecated as readily and with the same effect as other personal property. If ship mortgages are accorded such a status, there is ground for supposing that they can be employed more advantageously than heretofore" (R. 332).

The narrow and illogical construction placed upon the Ship Mortgage Act by the majority of the Circuit Court of Appeals will have the inevitable effect of largely impairing, if not completely defeating, the purpose of Congress in enacting the legislation. Purchasers of bonds secured by preferred mortgages will no longer be able to rest secure upon the assurance, which should follow from a strict compliance with the express provisions of the Ship Mortgage Act. For strict compliance will afford no assurance, since under the decision of the majority of the Court below, that assurance may be completely destroyed if the mortgagor testifies and the Court finds as a fact that the mortgagee (merely a Trustee for innocent bondholders) knew when the mortgage was given that a substantial part of the proceeds were to be devoted to non-maritime uses. It is obvious that the public will not purchase this type of security under such circumstances.

POINT II.

The Ship Mortgage Act is a valid exercise of the power granted to Congress under Article III, Section 2 of the Constitution.

Article III, Section 2 of the Constitution of the United States extends the judicial power to "all Cases of admiralty and maritime Jurisdiction."

Article I, Section 8 confers upon Congress power "to make all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers, and all other Powers vested by this Constitution in the Government of the United States or in any Department or Officer thereof."

In the case of *Panama Railroad Company v. Johnson*, 264 U. S. 375, in speaking of the constitutional grant contained in Article III, Section 2, this Court said at page 386:

> "Although containing no express grant of legislative power over the substantive law, the provision was regarded from the beginning as implicitly investing such power in the United States. Commentators took that view; Congress acted on it, and the courts, including this Court, gave effect to it. Practically, therefore, the situation is as if that view were written into the provision. After the Constitution went into effect, the substantive law theretofore in force was not regarded as superseded, or as being only the law of the several states, but as having become the law of the United States,—subject to power in Congress to alter, qualify, or supplement it as experience or changing conditions might require."

In the case of *The Lottawanna,* 21 Wall. 558, this Court said at page 577:

> "It cannot be supposed that the framers of the Constitution contemplated that the law should forever remain unalterable."

In the case of *Southern Pacific Company v. Jensen,* 244 U. S. 205, this Court said at page 215:

> "Considering our former opinions, it must now be accepted as settled doctrine that, in consequence of these provisions, Congress has paramount power to fix and determine the maritime law which shall prevail throughout the country."

Citations might be multiplied which establish that it is now beyond dispute that Congress has power in its discretion, and as required by experience or changing conditions, to alter, qualify or supplement the maritime law by statutes of general application embodying its deliberate judgment. Only thus may be safeguarded the characteristic of harmony and uniformity conferred by the constitutional grant. Through the exercise of such power is made possible the continued adherence by Congress to its fixed and time honored policy of encouragement and protection of investment in ships and the consequent maintenance and strengthening of our national merchant marine. It follows that Congress has power to create and confer preferred status upon a mortgage covering a vessel of the United States without regard to the uses which may be made of the proceeds of such mortgage.

The constitutionality of the Ship Mortgage Act was first attacked in the case of *The Oconee,* 280 Fed. 927.

It was there urged that it was beyond the power of Congress to give a preferred status to a ship mortgage upon the ground that a ship mortgage was a non-maritime contract, and that it was not within the power of Congress to create a preferred maritime lien out of a contract essentially non-maritime in character, citing as a basis for the claim the cases of:

The John Jay, 17 How. 399;
Peoples Ferry Co. v. Beers, 20 How. 393;
The J. E. Rumbell, 148 U. S. 1;
The Lottawanna, 21 Wall. 558, among others.

Both upon reason as well as upon the authority of the very cases cited, District Judge Groner, sitting in the Eastern District of Virginia, upheld the constitutionality of the Act.

The constitutionality of the Ship Mortgage Act was again attacked in the case of *The Nanking,* 292 Fed. 642, where the same considerations were urged as were urged in the case of *The Oconee, supra.* Judge Partridge, sitting in the Northern District of California, again upheld the constitutionality of the Act.

The constitutionality of the Act was again attacked, as well as the power of Congress to enlarge the admiralty jurisdiction of the District Court, in the case of *The Lincoln Land,* 295 Fed. 358. In this case Judge Brewster, sitting in the District Court of Massachusetts, again upheld the constitutionality of the Act, as well as the power of Congress to enlarge jurisdiction of the District Court, sitting in admiralty.

In the case of *Morse Dry Dock & Repair Co. v. Steamship Northern Star,* 271 U. S. 552, the constitu-

tionality of the Act was assumed by this Court, inasmuch as the question of constitutionality of the Ship Mortgage Act was apparently not raised.

This Court has, therefore, never interpreted the Ship Mortgage Act as a whole, nor considered the power of Congress to enact it.

The power of Congress to make substantive changes in the law maritime has been repeatedly exercised. The jurisdiction of the District Court, sitting in admiralty, by the Judiciary Act of 1789 (Act Sept. 24, 1789, Sec. 9, 1 Stat. 76) was made to include cases of seizure under the impost, navigation and trade laws. The original act providing for limitation of liability, enacted March 3, 1851 (Ch. 43, 9 Stat. 635, 636) made a radical change in the substantive law and the jurisdiction of a court of admiralty to enforce the provisions of the Act automatically followed. The Act of June 23, 1910 (Ch. 373, 36 Stat. 604) creating a maritime lien for supplies furnished in a home port of a vessel where no lien had theretofore existed under the general maritime law, automatically conferred jurisdiction on the District Courts to enforce such liens. Indeed, before Congress enacted the statute in question this Court held (Perry v. Haines, 191 U. S. 17) that where a State statute gave a maritime lien for supplies furnished in a home port of a vessel the District Courts of the United States had exclusive jurisdiction to enforce that lien by proceedings *in rem*—this to the exclusion of State statutes providing a remedy *in rem*.

By the Act of June 26, 1884 (Ch. 121, Sec. 18; 23 Stat. 57, 46 U. S. C. 189) Congress radically extended

the martime law by an addition to the Limited Liability Act by which the individual liability of a ship owner was limited to the proportion of any and all debts and liabilities his individual share of the vessel bore to the whole; and in *Richardson v. Harmon,* 222 U. S. 96, this Court held that the provisions of the Act in question extended to and included non-maritime torts, and that the owner of a vessel could proceed in admiralty for a limitation of his liability for the destruction of a bridge concededly a land structure. There was no express act of Congress extending the jurisdiction of the admiralty courts to non-maritime torts. Jurisdiction followed as a result of the enactment of the Act.

The instances cited sufficiently illustrate the power of Congress to extend the maritime law to matters essentially non-maritime in character. Indeed, the power of Congress so to do was expressly recognized in a dictum of the United States Supreme Court in the case of *The John Jay,* 17 How. 399, where it is suggested that Congress would have the power to extend the maritime law to cover a ship mortgage in the following language:

> "It is true that the policy of commerce and its exigencies in England have given to its Admiralty Courts a more ample jurisdiction in respect to mortgages of ships, than they had under its former rule, as that has been given in this opinion. But this enlarged cognizance of mortgages of ships has been given there by Statute 3 and 4, Vic., ch. 65. Until that shall be done in the United States, by Congress, the rule in this particular must continue in the Admiralty Courts of the United States, as it has been."

That Congress has complete power to control and regulate vessels of the United States was expressly recognized by this Court in the case of *White's Bank v. Smith*, 7 Wall. 646, where the Court said:

> "Some question is made as to the power of Congress over the title and property of vessels of the United States to such an extent as to enable it to pass a recording Act.
>
> But, after the regulation of this species of property by the several Acts of Congress to which we have referred, and in respect to which there has never been a question, there can be very little hesitation in conceding the power to protect the rights of subsequent *bona fide* purchasers and mortgagees therein.
>
> Ships or vessels of the United States are the creations of the legislation of Congress. * * *"

If Congress intended in the enactment of the Ship Mortgage Act that the application of the proceeds of a mortgage should be limited to maritime uses, it has defeated the primary purpose of the Act. If Congress intended to create a preferred mortgage lien without placing any limitation, express or implied, upon the application of the proceeds, it had undoubted power based upon both reason and authority so to do and the purpose of the statute is fully served.

POINT III.

If the mortgages in suit are preferred mortgages under the Act, the jurisdiction of the District Court over an action in rem to enforce them necessarily follows.

In the preceding point we have noted that in cases where Congress has extended the maritime law to

subjects over which the courts of admiralty had never theretofore exercised jurisdiction that jurisdiction automatically followed without any express enactment of Congress. Here, however, Congress, exercising superabundant caution, by the express provisions of Subsection K (41 Stat. 1003; 46 U. S. C. Sec. 951) has expressly vested jurisdiction in the District Courts in the following language:

> "Upon the default of any term or condition of the mortgage, such lien may be enforced by the mortgagee by suit *in rem* in admiralty. Original jurisdiction of all such suits is granted to the district courts of the United States exclusively."

If Congress has the power to make a ship mortgage, which prior to the enactment of the statute was concededly a non-maritime contract, a preferred mortgage lien, maritime in character, having priority over various other types of maritime liens, it likewise had authority to vest jurisdiction in the District Court, sitting in admiralty, to enforce that lien.

That Congress possesses adequate power to create a lien effective against vessels of the United States may not be questioned. Such instruments of commerce engaged in water transportation and navigation are always subject to the regulation and control of Congress. *White's Bank v. Smith, supra.* The creation of a preferred mortgage lien upon vessels of the United States is but a further employment of the power of Congress to regulate and control such instrumentalities of transportation and commerce.

The lien so created consists of an appropriation of the personified *res* as security for the indebtedness represented by the mortgage. Such has ever been the characteristic foundation of the *rem* action in the admiralty. Once created, the lien is exclusively enforceable against the personified *res* in a court of admiralty, and not elsewhere.

Such jurisdiction may only be defeated by the destruction of the preferred status of the mortgages. But preferred status attained through compliance with the conditions of the statute may not be here destroyed. Reference to the respective mortgages which are attached to and expressly made a part of the libels (R. 10, 63) shows that the mortgagor solemnly covenanted and engaged that all requisite corporate action on its part for the execution and delivery of the bonds and of the respective mortgages had been taken (R. 29, 82); that the mortgagor would, in all respects, comply with the provisions of the Ship Mortgage Act so as to create and maintain the respective mortgages as preferred mortgages within the provisions of the Act, and would perform such acts as requested by the Trustee, as reasonably calculated to preserve the preferred status of the mortgages until fully paid and performed (R. 32, 85). Moreover, Article XIII of the respective mortgages provides:

> "Preferred Mortgage.
>
> That the mortgagor shall comply with and satisfy all the provisions of the 'Ship Mortgage Act, 1920' and shall establish and maintain this mortgage as a first preferred mortgage under said Act" (R. 35, 88).

In the face of these covenants contained in the mortgages, the preferred status of the mortgages in suit cannot be destroyed and the jurisdiction of the District Court over actions *in rem* to enforce such preferred mortgages necessarily follows.

POINT IV.

Estoppel bars the defense and renders the testimony on which the majority opinion rests wholly incompetent.

If effect be given to the admissions contained in the answers and to the binding character of the affirmative covenants contained in the mortgages, the mortgagor was estopped from offering the testimony in question, either for the purpose of attacking the validity of the mortgages or defeating the jurisdiction of the Court. Notwithstanding the opinion of the majority of the Court below is based on this wholly incompetent testimony.

CONCLUSION.

We respectfully submit that a writ of certiorari should be granted to review the decisions of the United States Circuit Court of Appeals for the Second Circuit in these causes because of the importance of the questions presented which ought to be settled by this Court; because the decision in the present cases destroys the benefits provided by the Ship Mortgage Act in cases where strict compliance was had with the provisions of the Act conferring a preferred mortgage status; and because the decision in the present cases is contrary to both the letter and spirit of the Ship Mortgage Act.

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Respectfully submitted,

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